

## **APPENDIX C**

## CODE OF PROFESSIONAL RESPONSIBILITY OF THE SOCIETY OF FINANCIAL SERVICE PROFESSIONALS

The Code of Professional Responsibility of the Society of Financial Service Professionals is divided into five components, as follows:

- Preamble – a brief introduction to the Code of Professional Responsibility, including its history and purpose.
- Canons – aspirational model standards of exemplary professional conduct.
- Rules – specific standards of a mandatory and enforceable nature.
- Applications – practical examples of how the canons and rules apply in given situations.
- Disciplinary Procedures – the mechanisms for enforcement of the Code of Professional Responsibility.

### *PREAMBLE*

The Society of Financial Service Professionals is dedicated to setting and promoting standards of excellence for professionals in financial services. In fulfillment of this mission, the Society's Board of Directors has adopted this Code of Professional Responsibility. All Society members are automatically bound by its provisions.

The ultimate goal of enacting the Code is to serve the public interest. The path to fulfilling the goal is the fostering of professionalism in financial services. A profession has been defined in the writings of Solomon S. Huebner as possessing four essential traits.

- knowledge or expertise
- service to others
- working with other professionals to enhance the practice and reputation of one who is a member
- self-regulation

Through its Code of Professional Responsibility, the Society strives to improve the level of ethical behavior among its members by articulating standards that are aspirational in nature, that is, by identifying the lofty, altruistic ideals that define a true profession, and by delineating and enforcing minimum standards of ethical conduct.

This Code of Professional Responsibility has its origin in the code of ethics of the American Society of CLU & ChFC, the predecessor organization of the Society of Financial Service Professionals. The members of the Society created and adopted a code of ethics in 1961. With a name change in the fall of 1998, and a broadened membership constituency, it became appropriate to create this new Code of Professional Responsibility.

The Society acknowledges the diversity of its membership... from those that serve the public directly, as advisers, to those that serve indirectly through companies, educational organizations, and the like. Whatever role he or she plays within the financial services industry, it is the responsibility of each Society member to understand and adhere to the Code of Professional Responsibility.

From time to time, a Society member may be unclear about the ethical implications of a given course of action. In such cases, a Society member may request an advisory opinion from the Society, or may seek confidential advice through the Society's Ethics Information Line. Advisory opinions will be unpublished and specific to the inquiring member. However, there may be instances in which the subject matter of the advisory opinion has broad, general application and in such cases, at its discretion, the Society may choose to publish a given opinion for the benefit of all members, preserving the anonymity of those involved.

An alleged violation of the Society's Code of Professional Responsibility will result in an enforcement action, carried out in accordance with the Disciplinary Procedures. The procedures ensure that any member charged with ethical misconduct is afforded appropriate due process. The procedures also provide for appropriate sanctions, such as reprimand, censure, and revocation of membership, should a member be found to have acted in violation of the

Code.

True enforcement of ethical behavior must come from the personal conscience of each individual, rather than external forces. Nevertheless, as an organization that promotes its members' education and expertise to the consumer, the Society believes it is essential that it act in an enforcement capacity.

## CANONS

### **CANON 1 Fairness**

A member shall perform services in a manner that respects the interests of all those he/she serves, including clients, principals, partners, employees, and employers. A member shall disclose conflicts of interests in providing such services.

Fairness requires that a professional treat others as he/she would wish to be treated if in the other's position. A professional also strives to avoid unfairness by inflicting no unnecessary harm on others and, when possible, shielding others from harm.

### **RULES**

**R1.1** A member shall not engage in behavior involving concealment or misrepresentation of material facts.

#### **Applications for Rule 1.1:**

**A1.1a.** In the sale of financial products, the use of product projections that are more aggressive than the company's current assumptions – without offering alternate illustrations/projections using more conservative assumptions – is a form of misrepresentation. It is best to show a range of assumptions for each product to illustrate the impact of changes on the rate of return and other expenses.

**A1.1b.** To avoid misrepresentation, the financial services professional is advised to use unbiased historical illustrations, show past performance, and to educate the consumer on the difference between past results and projections, and actual future results.

**A1.1c.** Improper replacement is a form of misrepresentation. When considering the replacement of one insurance, annuity, or other financial product for another, a thorough comparison of both products, including surrender charges, incontestable clauses, expenses, fees, and tax consequences, should be completed. The Society's Replacement Questionnaire (RQ) provides a tool for the thorough analysis of replacement issues.

**A1.1d.** Failing to note a preexisting medical condition on an insurance application is a form of concealment.

**R1.2** A member shall respect the rights of others.

**R1.3** A member shall disclose to the client all information material to the professional relationship, including, but not limited to, all actual or potential conflicts of interest. In a conflict of interest situation, the interest of the client must be paramount.

#### **Applications for Rule 1.3**

**A1.3a.** A potential conflict of interest is inherent in the relationship between the client and the financial service professional when the professional is compensated by commissions on the sale of financial products. In such circumstances, if asked by the client or prospect, the professional should disclose, to the best of his/her knowledge, all forms of compensation, including commissions, expense allowances, bonuses, and any other relevant items.

**A1.3b.** The potential for a conflict of interest exists when a financial service professional receives fees for referring business to another practitioner. The referring professional should disclose this information.

**A1.3c.** A member who serves as a director or trustee of an organization/business faces a conflict of interest when

competing to provide product or services to this organization for compensation. For example, Jackie Jones, ChFC, a professional money manager, is on the board of XNet Corporation. XNet is currently interviewing candidates to manage its \$10 million investment portfolio. If Jackie decides to seek XNet's account, she is in a conflict of interest situation. Under these circumstances, Jackie should disclose the conflict to all relevant parties and have the parties acknowledge and accept the conflict. Additionally, Jackie should consider recusing herself from all discussions and decision-making regarding the selection of XNet's money manager. She may also consider resigning from the board or taking her name out of consideration for the money manager position.

**R1.4** A member shall give proper respect to any relationship that may exist between the member and the companies he or she represents.

#### **Application for Rule 1.4**

**A1.4a.** Society members frequently have contractual relationships with the company whose products they sell. Honoring the terms of these contracts and refraining from negative statements about such companies are examples of giving proper respect to the relationship. Note, however, the need to balance the requirements of Rule 1.4 with the duty to act in the best interest of the client.

**R1.5** A member shall make and/or implement only recommendations that are appropriate for the client and consistent with the client's goals.

#### **Applications for Rule 1.5**

**A1.5a.** Compliance with Rule 1.5 requires the financial service professional to use his/her best efforts to (1) understand the client's/prospect's personal and financial background and experience; (2) understand the client's/prospect's risk tolerance; and (3) educate the client about the various options available to meet identified needs and goals. This may include utilizing a fact-finding and/or risk assessment tool, one-on-one educational/counseling sessions, sharing newspaper or magazine articles, etc. In these circumstances, the financial service professional is cautioned against providing advice if he or she is not properly licensed or authorized to do so. See also Rule 2.2 and the Application A2.2a.

**A1.5b.** Appropriateness of the recommendation to the client's needs must take precedence over any sales incentives available to the financial service professional, such as conventions, trips, bonuses, etc. For example, Bob Bucks needs to sell just one more policy to qualify for MDRT. He knows he can convince his best client to purchase additional insurance coverage even though Bob knows the current coverage is more than adequate. If Bob makes this sale, he has violated Rule 1.5.

**R1.6** In the rendering of professional services to a client, a member has the duty to maintain the type and degree of professional independence that (a) is required of practitioners in the member's occupation, or (b) is otherwise in the public interest, given the specific nature of the service being rendered.

#### **Application for Rule 1.6**

**A1.6a.** The requirement of professional independence mandated by Rule 1.6 presents a special challenge for Society members who are contractually bound to sell the products of only one company, or a select group of companies. In such cases, the member must keep paramount his/her ethical duty to act in the best interest of the client, even if this means forgoing a sale.

### **CANON 2 Competence**

A member shall continually improve his/her professional knowledge, skill, and competence.

Professionalism starts with technical competence. The knowledge and skills held by a professional are of a high level, difficult to attain, and, therefore, not held by the general public. Competence not only includes the initial acquisition of this specialized knowledge and skill, but also requires continued learning and practice.

## **RULES**

**R2.1** A member shall maintain and advance his/her knowledge in all areas of financial service in which he/she is engaged and shall participate in continuing education programs throughout his/her career.

### **Application for Rule 2.1**

**A. 2.1a.** Compliance with Rule 2.1 requires, at a minimum, meeting the applicable continuing education standards set by state licensing authorities, the Society of Financial Service Professionals, the American College, the CFP Board of Standards, and any other entity with appropriate authority over the member's license(s) or other credentials. For example PACE, the joint CE program of the Society of and the American College requires 30 hours of CE every 2 years. The CFP Board of Standards also requires 30 hours of continuing education every 2 years for CFP® licensees.

**R2.2** A member shall refrain from giving advice in areas beyond the member's own expertise.

### **Applications for Rule 2.2**

**A2.2a.** A member shall not give tax, legal, insurance, accounting, actuarial, investment, or other advice unless the member has professional training and is properly licensed in these areas. For example, to avoid the unauthorized practice of law, the financial service professional will clearly mark specimen documents, such as living or testamentary trusts or buy-sell agreements, as samples and inform the client that the documents must be reviewed by a licensed attorney.

**A2.2b.** Billy Burke, CFP®, has a specialized financial planning practice that focuses on assisting clients with funding college for their children. When Billy's long-time client and friend, Margaret Hamilton, asks for help in managing the distribution of funds from her defined benefit plan, Billy knows this is beyond his area of expertise, but he doesn't want to let his friend down. Billy proceeds to recommend several investment options to Margaret, but neglects to mention the early withdrawal taxes and penalties. Billy has violated Rule 2.2.

## **CANON 3 Confidentiality**

A member shall respect the confidentiality of any information entrusted to, or obtained in the course of, the member's business or professional activities.

A financial service professional often gains access to client records and company information of a sensitive nature. Each Society member must maintain the highest level of confidentiality with regard to this information.

## **RULES**

**R3.1** A member shall respect and safeguard the confidentiality of sensitive client information obtained in the course of professional activities. A member shall not divulge such information without specific consent of the client, unless disclosure of such information is required by law or necessary in order to discharge legitimate professional duties.

### **Application for Rule 3.1**

**A3.1a.** Examples of sensitive client information include, but are not limited to, medical data, information about financial status, Social Security or credit card numbers, information about personal relationships, etc. In determining whether information is sensitive, the Society member should take a cautious approach, and if in doubt, discuss the issue with the client.

**R3.2** A member shall respect and safeguard the confidentiality of sensitive company/employer information obtained in the course of professional activities. A member shall not divulge such information without specific consent, unless disclosure of such information is required by law or necessary in order to discharge legitimate professional duties.

**R3.3** A member must ensure that confidentiality practices are established and maintained by staff members so that breaches of confidence are not the result of intentional or unintentional acts or omissions.

#### **Application for Rule 3.3**

**A3.3a.** A member who employs others who work with sensitive, confidential client information has the responsibility to train these employees in the handling of such information. These employees must be instructed that they will be held responsible for unauthorized disclosure of confidential data. For example, Judy Parker has set up detailed procedures for her staff to follow in safeguarding confidential client information. On three separate occasions, Judy overheard her office manager gossiping with friends about the size of Client X's investment portfolio. Judy has not taken any action in regard to the office manager's behavior. Judy has violated Rule 3.3.

#### **CANON 4 Integrity**

A member shall provide professional services with integrity and shall place the client's interest above his/her own.

Integrity involves honesty and trust. A professional's honesty and candor should not be subordinate to personal gain or advantage. To be dishonest with others is to use them for one's own purposes.

#### **RULES**

**R4.1** A member shall avoid any conduct or activity that would cause unnecessary harm to others by:

- Any act or omission of a dishonest, deceitful, or fraudulent nature.
- Pursuit of financial gain or other personal benefits that would interfere with the exercise of sound professional judgments and skills.

**R4.2** A member shall establish and maintain dignified and honorable relationships with those he/she serves, with fellow practitioners, and with members of other professions.

#### **Application for Rule 4.2**

**A4.2a.** A member needs to be respectful in all dealings with another financial service professional in competitive engagements and avoid at all costs defamatory remarks to the client or other professionals. This does not mean a member cannot provide impartial factual information about a competitor. For example, in trying to help a friend make a decision about which long-term care policy to purchase, Joe Carter, CLU, reviews the features of each contract and accurately notes that his competitor's policy fails to provide coverage for Home care. Joe recommends that his friend review this information with his agent.

**R4.3** A member shall embrace and adhere to the spirit and letter of laws and regulations governing his/her business and professional activities. See also Rule 6.1.

**R4.4** A member shall be truthful and candid in his/her professional communications with existing and prospective clients, and with the general public.

#### **Applications for Rule 4.4**

**A4.4a.** Financial service professionals will not use words or make statements in brochures or advertising materials or in any client communication that create false impressions or have the potential to mislead. For example, product salespersons should not refer to themselves as financial/estate planners/consultants, if they do not provide these services. Words such as deposits or contributions should not be used to describe life insurance premiums. Life insurance policies should not be referred to as retirement plans. Discussion of vanishing premiums and guaranteed performance should be avoided. Financial service professionals must avoid creating the impression that they represent a number of companies when they place business with only a few companies. (See also Rule 1.6.)

**A4.4b.** Candid communication is required when a client is acting or intends to act outside the law. In such cases, the member should terminate the professional relationship and seek the advice of appropriate advisers. For example,

Lisa Long, CLU, CFP®, an investment adviser, has been asked by her client to effect a transaction based on insider information. Lisa must immediately advise her client that insider trading is a violation of SEC rules and could result in criminal charges. Lisa should also document what has happened; and if, the client plans to proceed with the transaction, Lisa should terminate the relationship. Lisa should also consult her own legal and ethical advisers as to whether she has additional legal obligations under these circumstances. Lisa's legal obligations will impact her ethical obligations.

**R4.5.** A member shall refrain from using an approved Society designation, degree, or credential in a false or misleading manner.

#### **Application for Rule 4.5**

**A4.5a.** A member must not use Society-recognized professional designations in his/her company name, tagline, or brochures in a manner which would be misleading. For example, John Smith, ChFC, and Associates is acceptable. John Smith and Associates, Chartered Financial Consultants is not because it creates the impression that everyone associated with the firm is a Chartered Financial Consultant. (See Rule 7.7 also.)

#### **CANON 5 Diligence**

A member shall act with patience, timeliness, and consistency in the fulfillment of his/her professional duties.

A professional works diligently. Knowledge and skill alone are not adequate. A professional must apply these attributes in a prompt and thorough manner in the service of others.

#### **RULES**

**R5.1** A member shall act with competence and consistency in promptly discharging his/her responsibilities to clients, employers, principals, purchasers, and other users of the member's services.

**R5.2** A member shall make recommendations to clients, whether in writing or orally, only after sufficient professional evaluation and understanding of the client's needs and goals. A member shall support any such recommendations with appropriate research and documentation.

**R5.3** A member shall properly supervise subordinates with regard to their role in the delivery of financial services, and shall not condone conduct in violation of the ethical standards set forth in this Code of Professional Responsibility.

#### **CANON 6 Professionalism**

A member shall assist in raising professional standards in the financial services industry.

A member's conduct in all matters shall reflect credit upon the financial services profession. A member has an obligation to cooperate with Society members, and other financial service professionals, to enhance and maintain the profession's public image and to work together to improve the quality of services rendered.

#### **RULES**

**R6.1** A member has the duty to know and abide by the local, state, and national laws and regulations and all legal limitations pertaining to the member's professional activities.

#### **Applications for Rule 6.1**

**A6.1a.** The financial service profession is subject to state and federal laws and regulation in the areas of securities, insurance, banking, and unfair trade practices, among others. Society members must understand these laws and

regulations and their applicability to their practices. For example, Susan Short, CLU, just earned her CFP® license, and is planning on expanding her practice to include comprehensive financial planning services. Does Susan need to register as an investment adviser? Must she be licensed with the National Association of Securities Dealers? What about state insurance laws? Susan must answer these questions and comply with the appropriate requirements for her business activities.

**A6.1b.** Jon Planner receives equity commissions throughout the year. As part of a prearranged agreement, he transfers these commissions to the corporation for whom he works. Jon later learns that this is a violation of NASD rules and that commissions cannot be split with corporations. Jon is ethically obligated to correct this situation and to further educate himself on the rules and regulations applying to his business.

**R6.2** A member shall support the development, improvement, and enforcement of such laws, regulations, and codes of ethical conduct that foster respect for the financial service professional and benefit the public.

#### **Application for Rule 6.2**

**A6.2a.** Suppose Congress is contemplating a measure that would increase the regulatory burden on financial service professionals by requiring increased documentation of specific client transactions. There is firm evidence that enactment of this measure would substantially reduce the likelihood of client's being misled or confused about such transactions. Rule 6.2 would require Society members to support such a measure.

**R6.3** A member shall show respect for other financial service professionals and related occupational groups by engaging in fair and honorable competitive practices; collegiality among members shall not impede enforcement of this Code.

**R6.4** A member shall cooperate with regulatory authorities regarding investigations of any alleged violation of laws or regulations by a financial service professional.

### **CANON 7 Self-Regulation**

A member shall assist in maintaining the integrity of the Society's Code of Professional Responsibility and of the professional credentials held by all Society members.

Every professional has a responsibility to regulate itself. As such, every Society member holds a duty of abiding by his/her professional code of ethics. In addition, Society members have a duty to facilitate the enforcement of this Code of Professional Responsibility.

#### **RULES**

**R7.1** A member has the duty to know and abide by all rules of ethical and professional conduct prescribed in this Code of Professional Responsibility.

#### **Application for Rule 7.1**

**A7.1a.** Society members are advised to review the Code of Professional Responsibility at least annually.

**R7.2** A member shall not sponsor as a candidate for Society membership any person known by the member to engage in business or professional practices that violate the rules of this Code of Professional Responsibility.

**R7.3.** A member shall not directly or indirectly condone any act by another member prohibited by this Code of Professional Responsibility.



#### **Application for Rule 7.3**

**A7.3a.** If requested, a Society member should serve on such committees, boards, or hearing panels as are prescribed by the Society for administration or enforcement of the Code of Professional Responsibility. A Society member is obligated to disqualify him/herself from such service if he/she cannot not serve in a fair and impartial manner.

**R7.4** A member shall immediately notify the Society if he/she is found in violation of any code of ethics to which he or she is subject and shall forward details to the Society.

**R7.5** A member shall immediately notify the Society of any revocation or suspension of his/her license by a state or federal licensing or regulatory agency and forward details to the Society.

#### **Application for Rule 7.5**

**A7.5a.** If, after due process, a Society member is judged to have violated the code of ethics of another organization, he/she should notify the Society and provide such detail as may be necessary.

**R7.6** A member possessing unprivileged information concerning an alleged violation of this Code of Professional Responsibility shall report such information to the appropriate enforcement authority empowered by the Society to investigate or act upon the alleged violation.

#### **Applications for Rule 7.6**

**A7.6a.** If a member believes that another member of the Society may have violated the Code of Professional Responsibility, the Society recommends, where feasible, that direct communication between the two members be the first step in addressing the problem.

**A7.6b.** The Society's Code of Professional Responsibility places responsibility upon all members to report violations of this Code. (See also Rule 7.6.)

**R7.7** A member shall report promptly to the Society any information concerning the unauthorized use of an approved Society designation, degree, or credential.

#### **Application for Rule 7.7**

**A7.7a.** The Society logo may be imprinted on business cards and stationery used exclusively by the person who is a Society member. (See also Rule 4.6.)